

# **R O M A N I A**

MINISTRY OF PUBLIC FINANCE

POLICY PAPER

ON

PUBLIC INTERNAL FINANCIAL  
CONTROL

September 2005

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## **1. INTRODUCTION**

### ***1.1. Purpose***

The purpose of the Policy Paper is to establish the strategic short and medium term orientations of the public internal financial control in Romania.

### ***1.2. Objective***

The second edition of the Policy Paper has the objective of presenting the current situation of the Public Internal Financial Control system, as per the achievements since the last 5 years, to carry out a diagnosis and to design the main directions for future development of this system.

### ***1.3. Working Group***

This document has been up-dated by the MoPF –through its special directions Central Harmonization Unit of the Public Internal Audit and CHU-Financial Management and Control System, with the technical assistance from foreign experts.

The working group expresses its highest appreciation to all the actors that have contributed in various ways at the drafting and finalization of this document.

## **2. ABBREVIATION LIST**

PIA:	Public Internal Audit
DCB:	Delegated Controllers' Body
RCA:	Romanian Court of Accounts
PFC:	Preventive Financial Control
DPFC:	Delegate Preventive Financial Control
CoA	Court of Accounts
PIFC:	Public Internal Financial Control
OPFC:	Own Preventive Financial Control
CHU-PIA	Central Harmonization Unit of the Public Internal Audit
CHU-FMC	Central Harmonization Unit for the Financial Management and Control System
GDPF:	General Directorate for Public Finance
MoPF:	Ministry of Public Finance

### **3. DEFINITIONS AND CONCEPTS**

The Annex no. 1 contains the general definitions and concepts regarding the internal audit control used in the present document.

## **4. PUBLIC FINANCIAL CONTROL ENVIRONMENT IN ROMANIA**

At present, the Romanian public financial control environment is structured as follows:

### **4.1. Court of Accounts**

The Court of Accounts controls the way of creating, administrating and using the financial resources of the state and of public sector, being the public authority of the state that carries out the external audit in the public sector

The Court of Accounts functions near the Parliament and it carries its activity independently according to the Constitution and the laws of the country. The Court of Accounts is a professional independent institution, the account counselors being appointed by the Parliament for a 9 years mandate and they are revoked only by the Parliament. The members of the Court of Accounts are independent and irremovable during their mandate.

The Court of Accounts presents annually to the Parliament a report on the management accounts of the national public budget of the previous tax year, and the results of the evaluation of the financial management and control systems. The litigations aroused from the control activity are solved by the specialized courts of law.

### **4.2. Ministry of Public Finance**

#### *4.2.1. PIFC structures*

The structures of PIFC will be detailed in chapter 5.

#### *4.2.2. Fiscal Administration*

The determination, registration of debts, collection and following-up of collecting the due taxes and revenues are activities organized through the fiscal administration territorial network. The fiscal control, as an important component of establishing the obligations, is designed to evaluate the statements on fiscal duties of the taxpayers, and intends to eliminate the tax evasion. It is carried out by specialized structures at both central and territorial level.

#### *4.2.3. Public Treasury System*

The public revenues are collected and accounted through the Public Treasury System, on each particular taxpayer and on each revenue source, establishing the way in which the fiscal duties have been observed (level, deadlines etc.).

The public expenditures are also carried out through the Public Treasury System on the basis of the revenue and expenditure budgets of the public institutions. The Public Treasury controls the availability of credits (chapter, title) and the regularity of the payments, based on justifying documents (payrolls, invoices, work files etc). The Public Treasury is making annually and

quarterly , the account of the state budget execution, the budgets of the special funds and the local budgets, using a centralized accounting system.

#### *4.3.1. National Customs Administration*

The National Customs Administration has as objective to control the merchandise, the vehicles and the persons in the customs services at the border and in the territory, in order to calculate and collect the sums due as customs duties and other related public revenues (excises, VAT etc); it organizes and implement activities regarding prevention and fight against customs fraud and smuggle.

The National Customs Administration assures the homogeneously, impartial, transparent and non-discriminatory custom laws implementation to all natural and legal persons, regardless of their legal status and their organization and functioning structure.

#### *4.3.2 Financial Guard*

The Financial Guard exercises operational and unannounced inspections in order to prevent, to detect and to fight against any actions and deeds in the economical, fiscal and customs field, which might have as a result tax evasion and fiscal fraud.

#### *4.3.3. Other control authorities*

There are other control authorities in specific fields of activity which act in order to prevent, to establish and to sanction the law infringement as: National Environment Guard, State Inspectorate for Buildings, Labor Inspection, Veterinary and Sanitary Inspection etc.

### **4.4. Prime Minister's Office**

The Prime Minister's Office is a structure of the Government body which performs also controls ordered by the Prime Minister on the activity of both central and local authorities and public institutions.

The Prime Minister's Office in its role of contact point to the European Office of the Antifraud Fight.(OLAF) assures the coordination of the antifraud fight and the protection of the EU's financial interests in Romania.

### **4.5. The financial control system of local communities**

The commitments and disbursements from the local community budget are the responsibility of the main spending center(the major).

The establishment of the local budget revenues, as well as collecting, following-up and controlling the reliability of the fiscal duties and the local tax statements will be performed by special structures of the local councils.

The revenues are cashed and centralized through the Public Treasury System on each taxpayer and on each source of income, presenting the way in which the fiscal duties have been observed (level, deadline etc.)

The payments are made through the Public Treasury, which controls the credit reserves and their regularity based on justifying documents (invoices, cash situations, payrolls, etc.)

The structures of PIFC will be presented in the chapter 5.

## **5. CURRENT SITUATION OF THE PUBLIC INTERNAL FINANCIAL CONTROL**

### **5.1. Purpose of the Public Internal Financial Control**

The purpose of PIFC, as defined by the law, implies the verification of the legality, regularity and conformity of operations, identifying the weaknesses of the internal control system that had generated errors, misadministration or embezzlement and to propose measures to remedy these aspects. The PIFC is exercised in the following areas:

- Public revenues (determination, registration of debts and follow-up of collecting the revenues);
- Public expenditures managed by the main, secondary and third spending centers of the state budget, state social insurance budgets, extra budgetary funds, as well as of local communities budget;
- The use of external reimbursable and non-reimbursable public funds including the European Union's funds;
- The revenues and expenditures of national companies, national companies and other private legal bodies using public funds and/or which administrate the public patrimony.

### **5.2. General Legal frame-work for the Public Internal Financial Control**

The General Legal framework for the Public Internal Financial Control is presented in the Annex no. 2.

### **5.3. Types of Public Internal Financial Control**

#### *5.3.1. Internal Audit*

##### 5.3.1.1. Public Internal Audit

**Definition – concept:** the existing legal framework defines PIA as a functional, independent and objective activity, which assures and counsels the management in order to have a good administration of public revenues and expenditures, improving the activities of the public institutions; PIA helps the public entity to achieve its objectives by a disciplined and systemic approach which evaluates and improves the efficiency and the effectiveness risk based management system, control and governance process .

**Coordination:** MoPF, through CHUPIA, assures the coordination of the activity of public internal audit, by the followings:



- Elaborating, managing and implementing a harmonized strategy in the field of public internal audit; it monitors this activity at the national level.
- Developing and amending the relevant legislative framework.
- Developing and implementing uniform procedures and methodologies based on international standards agreed by the European Union, including internal audit manuals and audit trails.
- Developing risk management methodologies.
- Developing the Ethical Code of the internal auditor.
- Endorsing the methodological norms on PIA, specific to the different domains of activity in the field of public internal audit.
- Developing a reporting system for the results of all public internal audit activities and elaborating an annual report.
- Performing audit missions of national interest with multi-sectoral implications.
- Verifying whether norms, instructions, as well as the Ethical Code are respected by internal audit services in public entities; it may initiate the necessary corrective measures in co-operation with the Head of the respective public entity.
- Co-ordinating the system of recruiting and training in the field of public internal audit.
- Endorsing the appointment/dismissal of the Heads of internal audit services within the public entities.
- Co-operating and exchanging information with the Court of Accounts, as well as with other institutions in Romania;
- Co-operating with public financial control authorities and organisations in other countries, including the European Commission.

Along with the CHUPIA, it has been established the Committee for Public Internal Audit (CPIA), a consultative body, which works for defining the strategy and improving the internal audit activity, in public sector. In order to accomplish its objectives, CPIA has the following main attributions:

- Discussing the strategic development plans of the system of internal financial control and issuing an opinion on its development trends;
- Discussing and issuing an opinion on the legislative framework elaborated by the CHUPIA in the field of public internal audit;
- Discussing and issuing a consultative note on the annual report on the public internal audit activity and submitting it to the Government;

- Endorsing the annual audit plans of public internal audit of national interest with multi-sectorial implications;
- Discussing and issuing an opinion on the reports of public internal audit of national interest with multi-sectorial implications;
- Analyzing the importance of the recommendations expressed by the internal auditors in cases of divergent opinions between the Head of a public entity and its internal auditors and issuing an opinion on the consequences of not implementing the recommendations of the internal auditors;
- Analyzing the co-operation agreements between the internal audit and the external audit referring to the definition of the concepts and the use of standards in the field, the exchange of the results from the audit activity, as well as the common professional training of the auditors;
- Endorses the appointment/dismissal of the director of the CHUPIA,

In each public institution the audit activity is organized as an independent structure, directly under the subordination of the head of the public institution and, according to its attributes, it must not be involved in the process of elaborating the procedures of the internal control and in the activities which are subject to internal audit.

The attributions of the public internal audit unit are the following:

- ◆ elaborates the methodological norms specific to the public entity where it functions, with CHUPIA's endorsement or the approval of the hierarchical superior body for the subordinated public entities;
- ◆ drafts the Annual public internal audit Plan
- ◆ carries internal audit activity in order to evaluate if the managing, financial and control systems are transparent of and if they comply to the norms of legality, regularity, economy, efficiency and effectiveness.
- ◆ informs CHUPIA about the recommendations unaccepted by the head of the public entity and their consequences;
- ◆ periodically reports on the findings, conclusions and recommendations resulted from the audit missions;
- ◆ drafts the Annual Report on the public internal audit activity;
- ◆ reports immediately to the head of the public entity and to the designated internal control body about the law infringements and the possible damages identified.

In small public entities, which are not subordinated to other public entities, the public internal audit is reduced to compliance audit and is carried out by the public internal audit units of the Ministry of Public Finance from the territorial level.

The statute of the internal auditor.

The statute of the internal auditor is based on the principle of independence, being regulated by the Chart of Internal Audit, the Code of Ethics of the internal auditors as well as the professional norms applicable in Romania, having the following characteristics:

- the internal auditors are not subject to the management influence in designing the strategic and annual plan as well as in planning the ad-hoc audit missions. The internal auditors has the freedom to establish the priority areas to be audited base on risk analyses and to take into account the possible suggestions of the management.
- The internal auditor selects the types of audit he/she considers the most appropriate for the situation, i.e. compliance audit, system audit or performance audit.
- The conclusion and the recommendations of the internal auditor are the results of his/her own professional judgment
- The internal auditor reports to the head of the public entity, namely the highest decisional level
- In the case that the head of the public entity does not approve the conclusions and recommendations of the internal auditor, then the internal audit unit reports to CHUPIA for reconciliation. If the reconciliation does not work, the it is informed the Government
- For the actions carried out with good intentions in exercising its duties and within its limits, the internal auditors cannot be sanctioned or removed in another post
- The appointment/ dismissal of the internal auditors by the head of the public entity is done with the favorable endorsement of the chief of the internal audit unit, while its appointment/dismissal is done with the endorsement of CHUPIA

### **The carrying out of the audit activity**

The audit activity is carried out based on the annual audit plan, approved by the head of each public institution .The plan includes the selections of the audit unit. These plans cover all the activity of the institution and the auditor selects those with high-risk. In drafting the plan, the auditor has to take into account also the recommendations of the Court of Accounts and of CHUPIA. Each audit mission included in the audit plan is carried on based on the methodological norms and is finalized with an audit mission report. The Report is based on the relevant justifying documents. The report is presented to the auditee and the recommendations are submitted for approval to the head of the public entity. For the approved recommendations, the auditee structure has to elaborate action plans in order to implement the recommendations .

#### *5.3.2. Preventive Financial Control*

**Definition:** As defined by the existing legal framework, the Preventive Financial Control is an independent activity organized and performed in a public institution, consisting of systematic verification of the project operations, which imply financial decisions. The verification regards the legality, regularity and limitation within the established budgetary commitments of the transactions subject to control.

The transactions subject to the PFC refers to:

- ◆ budgetary credits and legal or commitments credits;
- ◆ opening and distribution of the budgetary credits;
- ◆ amendment of the quarterly distributions and on subdivisions of the budgetary classification of the approved credits, including credit transfers; bidding the expenditures;
- ◆ the creation of the public revenues, in order to authorize and establish the cash deed;
- ◆ reducing, spreading out or canceling the cash deeds;

- ◆ creation of the own resources of the EU budget, representing Romania's future contribution to this budget;
- ◆ to recover the advanced amounts of undue money
- ◆ sells, pledges, license or rent of the state private domain goods or territorial-administrative private domain goods;
- ◆ license or rent the state public domain goods or territorial-administrative public domain goods;
- ◆ other operations established by ordinance of the public finance ministry.

The PFC is exercised by granting the visa, respective refusing the visa.

**Co-ordination:** The MPF is the competent institution to ensure the co-ordination of the PFC activity through:

- continuous the developing and improvement of the legal framework;
- developing the general framework of the operations subject to the PFC and the methodological norms of exercising this type of control;
- endorses the specific methodological norms regarding the organization and the carrying out of the OPFC drafted by the main spending agencies of the state budget, of the state social insurance budget, of the special budgets and of the National Fund operations and of the Implementating Agencies which use community funds;
- drafts the annual national report on the PFC;
- coordinates the systems of professional training of the PFC.

**Organization:** The PFC is organized and exercised in two forms: own preventive financial control (OPFC) and delegated preventive financial control(DPFC)

### **5.3.2.1 The Own Preventive Financial Control**

The OPFC is organized in all the public institutions, usually within the financial-accountant units.

The operations subject to the control are those included in the general framework (established by the norms of MPF) completed with the specific operations of the public institution (established through a decision of the head of institution).

The person who exercises the PFC must not be involved in carrying the operations subject to the control.

The person exercising the PFC must not be imposed in any way to grant or to refuse the visa.

The persons appointed to carry out the OPFC have the responsibility of the respective operations according to their own contribution to it.

In case of visa refusal, the head of the institution can order the continuation of the operation on his own responsibility, but the Court of Accounts, the MoPF and the hierarchical superior body of the public entity have to be informed.

The evaluation of the own preventive financial control is done by the internal audit unit of the public institution.

The appointment /dismissal of the own preventive financial controllers is the responsibility of the head of the public institution, with the approval of the superior hierarchical body. The MoPF approval is needed only for the own preventive financial controllers from the main line ministries.

There is a legal framework for the OPF Controllers which provide a stimulating salary system.

#### **5.3.2.2. Delegated Preventive Financial Control**

The DPFC is organized and performed by the MoPF through the Delegated Controller's Body (DCB) which functions as a separate department subordinated to the minister of public finance. The DCB is managed by a Chief Financial Controller and two deputies, appointed by a Government Decision for a 6 years period .

The DCB, a structure of MPF, is organized independently of the management of the public entity in which it performs the visa.

The DPFC is performed as follows:

- a) to all main public institutions (main spending agencies, State Treasury, Public Debt, National Pre-Accession Fund and Implementing Agencies;
- b) in the case of high risk transactions, at other public institutions or private legal bodies managing public funds and/or administrating public patrimony.

The operations subject to the control are those included in the general framework established by MPF's norms completed with high-risk operations.

The visa refusal of the delegated controller, issued following a specific procedure, does not mean stopping the financial transactions, these ones could be performed based on the responsibility the head of the main spending agency, but being informed the MoPF and the Court of Accounts.

The evaluation of the delegated controller's activity is made annually by qualifications, based on the annual reports on the activity of the delegated controllers, on the evaluation of the internal audit unit of the MoPF and on the reports of Court of Accounts .

The DPF Controllers have a legal framework which compensate their responsibility with an adequate salary system.

### 5.3.3. Financial Management and Control Systems

According to the legal frame-work, MoPF is the central public administration authority which has the responsibility of drafting and implementing the policy in the field of finance administration. The MoPF provides methodological guidance, coordination and supervision of the assurance of the sound financial management on public funds and public patrimony administration.

By setting up the CHU-FM&CS within the MoPF, there have been created the possibility of a specialized body that assures the coordination of the FM&C over the following:

- defining an unitary strategy in the area of FM&C
- drafting the standards of the internal control
- harmonizing the methodological norms with financial implications by including control procedures for assuring the sound financial of the public funds and patrimony
- co-ordinating the training system of the specialists involved in the financial management and control
- developing a reporting system of the results of the activity of internal control

#### 5.3.4. Basic Internal control at the public entities

Romania agrees and uses elements of control framework proposed by the COSO model; when this model is implemented at the level of the public entity, it allows to administer better the activities for achieving the objectives.

The 5 elements of the COSO model are:

- a *The existence of a favorable control environment* , represents the attitude of the entire employees of the organization, including of the high level management over the internal control, by accepting, using and assessing it.
- b *Evaluating the risk*: the activities of public entity are permanently subject to internal and external risks that could lead to non achieving the objectives. The evaluation of the risks allows their prioritization for identifying unacceptable risks, the public entity must create internal control systems in order to minimize unacceptable risks and to maintain at an acceptable level the risks.
- c *Control activities*: In every field, the management of the public entity should use also other forms of internal control in order to limit or to eliminate the risks; these are the followings:
  - *self-control of the activity* – the compliance of every employee with their own working procedures;
  - *mutual control* – experienced between the procedural steps by every working level on the processing activities within the previous working level in order to add his own processing and to prepare the control which will be made by the next working level;
  - *hierarchical control* – realized on each responsibility level;

These three forms of control are carried out permanently over all activities of the public entity, the entire personnel being involved in this process. For the above mentioned forms of control there are no formalized procedures.

Along with these basic forms of internal control, which are incorporated to the activities of the public entity, of the preventive financial control and internal audit, the management of the public entity has the competency of establishing, when the situations ask for these forms of control, of which the most used are :

- *inspection*- which is launched as a result of some signals on potential irregularities and it consists of examination of documents, deeds, the assets, etc. with the purpose of establishing the deviances from the legal frame, of taking the measures for protecting the use of funds and public patrimony
- *patrimonial control* has as an objective the verification of the existence, integrity, preserving and the safeguarding of the goods and values.

These forms of control are based on distinct procedural rules, specific structures for performing it and a limited period of time.

- d *informing and communicating* – have the purpose of connecting separate control elements so that the results of it should be known by all of them who- directly or indirectly- will have to implement them. The lack of an efficient communication leads to a weak perception of the risks and consequently to design an inadequate control.
- e *Monitoring* is a process that assesses the performance of the internal control and it is exercised by the management by continuous supervising and periodic evaluation.

#### **5.4. Organization of PIFC on EU's Funds**

- The PIFC organizational structure in Romania implemented in the entities that run community funds , namely the National Pre-Adhesion Fund (NPAF) , CFCU- Central Financing and Contracting Unit, as well as the implementing and management agencies organized at the level of the ministries and national companies is the following:
  1. Own Preventive Financial Control made by persons appointed from the financial-accountant department. All the financial operations regarding the commitments and payments are subject to control;
  2. Delegated Preventive Financial Control made by a delegated controller, appointed by the minister of public finance, for each implementation structure; All the financial operations regarding the commitments and payments are subject to control over a certain value level (determined on the risk analysis) are subject to control;
  3. basic internal control
  4. Other control systems established by the head of the public entity
  5. Public Internal Audit, performed by the own audit units;



## **6. ANALYSIS OF THE PIFC IN ROMANIA**

The current situation of PIFC in Romania regarding both public national funds and EU'S funds have been described In the Chapters 4 and 5.

Based on this situation a critical analysis of the current situation can be made, highlighting both the strong and weak points of the current situation, as follows:

### **6.1 .Strengths of the current PIFC systems**

The present situation of the PIFC contains a series of strengths that represent the basis for its further development, according to EU requirements and practice. These strengths are the following:

1. the creation of the legal framework for implementing the PIFC in Romania , by designing and entering into force of Government Ordinance 119/1999 on the internal control and preventive financial control, Law no. 672/2003 on internal audit;
  - *consequence* the existence of the legal framework on organization and functioning of PIFC
2. The basic PIFC structures have been set up by the Government Ordinance 119/1999 regarding the internal control and preventive financial control, approved, modified and completed by Law no. 84/2003 and by Law no. 672/2003 on internal audit;
  - *Consequence:* PIFC has an organizational network, both at the central level and at the territorial level, which ensures its operational characteristic nation wide.
3. From the methodological and procedural point of view, there are operational norms, manuals and check-lists for the preventive financial control and for the internal audit.
  - *Consequence:* these control systems function effectively and assure systematically the protection of the public funds (including the community funds) and the public patrimony.
- 4 providing the mechanisms for training of the personnel from the PIFC system, both by Phare Technical Assistance, on internal control and internal audit and by developing the national system, respectively NIA and the School of Public Finance.
  - *Consequence:* the theory and the practice of PIFC in Romania is harmonized with the international; standards for control and internal audit and the best European practice
5. the structures of PFC and PIA are complying to the principle of functional separation, respectively they are not involved in the administrating and carrying out the audited/controlled activity at the spending agencies:

- consequence: it is assured one of the main principle, respectively the objectivity in the functioning of the two structures.
6. The Romanian system of PIFC performs the conditions of safeguard and efficiency of the pre-accession financial instruments for PHARE, SAPARD and ISPA.
    - *Consequence*: the efficient use of the Community funds is protected by the Romanian PIFC system .
  7. It has been started the process of integration the financial control into the managerial accountability, based on specific criteria and procedures that were approved by the Minister of finance
    - *Consequence*: there have been created the prerequisites for the total transfer of the preventive financial control into the managerial accountability.

## 6.2. The weaknesses of the current PIFC systems

The current situation of PIFC in Romania contains a series of weak points, which hinder the optimum functioning of this important form of control that have to be solved, both in short term and medium term.

These weaknesses are the following:

- a the unclear definition of the forms of internal control, that are components of the legal framework as presented at point 5.3.4 and 5.3.5
  - *Consequence*:
    - confusions between the functions of the internal control and internal audit
    - different perceptions at the managerial level on what it means “other forms of control
    - the tendency of the management to look for other forms of control ( inspections, patrimonial controls,) and less for those forms of control included in the procedures corresponding to the activities
- b insufficient understanding of the heads of the public institutions on their responsibility on establishing and maintaining functional the FM&C systems.
  - *Consequence*: low interest of the managers for setting up a performant FM&C system.
- c Lack of the structures at the level of central public entities that should provide the harmonization of the of the FM&C systems
  - *Consequence*: the functionality of the of the FM&C systems it is limited and it is not assisted by specialised staff

- e of the norms for regulating the internal control at the level of the public institutions
  - e Consequence: lack of an important component of the internal control system
- f insufficient development of the general methodology for carrying out system and performance audit
  - Consequence: in practice, system and performance audit are not carrying out yet.
- g The existence of a large number of small audit structures (1-2) territorially dispersed
  - Consequence: insufficient concentration of the audit resources that do not permit achieving a critical mass for carrying out adequately the internal audit activity
- h Partial functionality of the IT system for PIFC. The information sub-system for the FM&IC is under the design phase.
  - Consequence: low efficiency in monitoring the functionalities of the FM& C systems

## **7. NOTES AND PROPOSALS FROM EUROPEAN COMMISSION REPRESENTATIVES**

The defining of the PIFC system in Romania has been constantly monitored by the European Commission, that through its representatives have formulated a series of recommendations to harmonize them with the international standards of internal control and internal audit and the best practice in EU.

The recommendations, with major impact and whose implementation implies running a strategic plan, are the followings:

- a A coherent and harmonized development of the FM&C systems based on the principles and functions of managerial accountability
- b focusing the activity of the CPIA on debating and issuing a professional opinion on the main components of the strategy of internal audit in Romania ( strategic and annual planning , the independence of the internal auditor, professional training, assuring the quality of the internal audit and so on)
- c the flexibilization of the general methodological framework for carrying out internal audit missions in order to increase the functional independence and the professional judgment of the internal auditors (This recommendation has been made by Sigma's 2004 Peer Review, considering that a high level of formalization/standardization of the methodological norms, documents, circuits, responsibilities, periods of time, etc, can limit the initiative of the internal auditors during their audit missions.
- d Concentration of the internal audit resources by reducing the present territorial dispersion of small audit units (1-2 internal auditors), the weight should go on achieving a functional audit capacity and less on setting up new audit units.
- e Identifying the training needs and establishing the qualification criteria for internal auditors; in this process CHUPIA should play an important role.\

- f Developing the cooperation between CHUIA and Court of Accounts in order to increase the level of complementarity between the external and internal audit.

## **8. THE STRATEGY IN THE FIELD OF PUBLIC INTERNAL FINANCIAL CONTROL IN ROMANIA**

The modernization of the PIFC-system in Romania according to the new European concepts, internationally accepted, based on the development of a control and internal audit system able to ensure sound financial management systems for public funds and administering public patrimony, including the communitarian funds.

### **8.1. Strategic Objectives**

The strategy in the field of PIFC in Romania aims to achieve mainly the objectives mentioned below, in order to harmonize with the Community acquis-

- 1) A coherent and comprehensive legal basis which should include:
  - Principles and functions of the managerial accountability; obligations of the manager to establish and maintain the financial management and control systems and internal audit
  - the organization and the functions of the decentralized internal audit, that it will be carried out along with the classical financial audit, system audit and performance audit according to the recognized international standards. The internal auditor will become a counselor for the manager who evaluates the financial system of management and control and who will offer solutions for improving these systems;
  - the functions and the principles of organization of the FM&C systems should assure the management of the public entity, that the objectives of the organization are achieved through a sound financial management of the public funds, respectively in conditions of compliance, efficiency and effectiveness
- 2) Developing the methodologies and procedures for control and internal audit in order to harmonize it with the international standards and the best EU practice
  - promoting the standards for internal control for the public sector, based on COSO model
  - drafting the practical guides for implementing the standards for internal control
  - improving the general norms for carrying out the internal audit activity by increase the flexibility of the norms to give value to the initiative and professional judgment of the internal auditors
  - Defining the audit trails for the basic financial transactions of the public entity

- Drafting the manuals/practical guides for carrying out the internal audit missions for the support functions of the public entity
- 3) Strengthening the role of CHU-FM&C systems – a distinct structure within the MoPF by means of:
- Developing the reporting system of the results of the internal control activity and drafting the Annual Report, that will be submitted to the Government
  - Drafting of manuals, procedural guides on internal control
  - Developing of methodologies in the area of managerial risk
  - Formulating of proposals for improving the legal framework , to assure to the CHU-FM&C system the role of :
    - Monitoring and methodological guidance of the structures responsible in the area of internal control from the public entity, mainly in the direction of implementing the FM&C systems, of their harmonization
    - Harmonizing the methodological norms with financial implications, drafted at the level of the line ministries, from the point of view of control procedures in order to assure the sound financial management of the public funds and patrimony.
    - Monitoring the procedures of the budgetary programming and execution, at the level of the public entities
  - Drafting the Code of Ethics for the personnel involved in the FM&C
- 4) The organization of the units of FM&C at the level of the main central institutions that should carry out exclusively the functions of harmonization, monitoring, and methodological guidance, following that the executive functions to be carried out at the decentralized level by:
- Assuring and following the drafting of the procedures and guides for each unit from the structure of the public entity, of the specific norms on FM&C
  - Harmonization of the specific norms on FM&C of the procedures and guides from the coordinated structures
  - Quarterly reporting to CHU-FM&CS on the way of carrying out the internal control for the own activity of the central and local public institutions and of the subordinated entities, respectively the Local Councils.

The activity of the units for harmonization of FM&C will be guided, monitored and technically assisted by the CHU-FM&CS. (These structures are planned to be operational in a limited number of central public institutions –maximum 15 – that have in their responsibility drafting the specific procedures for public funds administration)

- e Improving the organization of the structures of internal audit by concentration of the audit resources and reduction of territorial dispersion. This action is carried out gradually, under the evaluation process of the audit activity, for all the central public institutions.
- f Gradually integration of the PFC into the sphere of managerial accountability, as the managerial control will ensure the elimination/minimizing of the risks in the administration of public funds, by strengthening the functional independence and increase the level of professional training of controllers, as well as by the guidance done by the DCB
  - OPFC it is exercised at all public entities on the projects of the transactions established by the management, based on risk analyses.

## **9. CONCLUSIONS**

By achieving the strategic objectives included in this document, it will be achieved a modern and efficient PIFC that will ensure a sound management of public funds including of the communitarian funds. This document will be subject to changes and updates whenever necessary.

The MPF approves this document and will take all the necessary measures in order to obtain the Government approval on the proposed strategy.

The content of this document will be basis of elaborating a normative document approved by the Parliament, taking into account the harmonization to the international and UE control and audit standards.

The normative document will most of all underline the central role of the internal audit as an independent evaluator of the control and financial management systems from the public units and as the manager's adviser. It will also show the manager's responsibilities regarding the establishing and maintaining a correct financial management in his field. The normative document will also contain elements of the harmonized procedures for all public units in order to approve or to refuse the preventive financial control, for the harmonized procedures in internal control field, for the Central Unit for Harmonization within MPF and for issuing manuals and guide procedures.

In Annex no.3 is established the schedule of implementation of the measures contained by the Developing Strategy of PIFC in Romania.

## **10. HUMAN, FINANCIAL AND MATERIAL MEANS NECESSARY FOR THE ACHIEVEMENT OF STRATEGIC PIFC OBJECTIVES**

### **10.1 Material means**

The establishment of an integrated computer system covering PIFC and including:

- commitment accounting; legislative data base; PIFC activity management; determination and design of significant samples for the identification of high risk operations (advanced control).•

Requirements: hardware (already for 80% achieved), application software and a communication system.

### **10.2. Human Resources Requirements:**

1. For generalization of PIA and inspection structures within the public entities 500 persons
- 2 For the deconcentration of preventive financial control:
  - Delegate controllers – for the working of the decentralized system (5 per county x 41 counties) : 205 persons;
3. For professional training:
  - training of trainers in 5 area centers: 15 persons;

### **10.3. Financial Requirements:**

- implementation of the computer system 2 MEURO
- expansion of the School of Public Finance network 1 MEURO
- financial resources for additional staff, introduced in the Public Internal Financial Control system  
1MEURO/year

**ANNEX NO. 1**  
**DEFINITIONS AND PLURAL CONCEPTS**

<b>Term</b>	<b>Definition</b>
Activity self-control	It is a form of control performed by the each employee at his working unit based on learning, understanding and fulfilling the tasks appointed by the manager or by the job requirements, by a permanent self evaluation of his own results and correcting the potential errors. It does not imply additional costs and can be very efficiently.
Audit Trail	It requires the maintenance of records giving the full documentation and justification at all stages of the life of a transaction together with the ability to trace transactions from summarized totals down to the individual details and vice versa. The overriding objective of the audit trail is to ensure a 'satisfactory audit from the summary amounts certified to the Commission to the individual expenditure items and the supporting documents at the final beneficiary'.
Auditing Standards	Auditing standards provide minimum guidance for the auditor that helps determine the extent of audit steps and procedures that should be applied to fulfill the audit objective. They are the criteria or yardsticks against which the quality of the audit results are evaluated.
Economy	Minimizing the cost of resources used to achieve given planned outputs or outcomes of an activity (including having regard to the appropriate quality of such outputs or outcomes).
Effectiveness	The extent to which objectives of an activity are achieved i.e. the relationship between the planned impact and the actual impact of an activity.
Efficiency	Maximizing the outputs or outcomes of an activity relative to the given inputs.
Ex ante financial control (preventive control) (EAFC)	Ex ante financial control (EAFC) is the set of control activities prior to carrying out financial decisions relating to appropriations, commitments, tender procedures, contracts (secondary commitments), and related disbursements and recovery of unduly paid amounts.
Financial Audit	Refers to examination and reporting the financial statements and the examination of the accountant statement on which is made the financial statements.
Functional Independence (FI)	The special status of a financial controller (narrow sense) or an internal auditor (whether central or decentralized), providing him/her with the power of maintaining a free professional judgment vis-à-vis his superior of the organization in matters of control and audit. FI should be embodied in relevant legislation way to ensure FI to allow the Internal Auditor (in case of conflict of interests) to report his findings freely to the central



	audit body.
Independence	From an internal audit viewpoint it means that the internal audit service should be organized directly under the top management. Nevertheless, the internal audit service should be free to audit any area that it considers to be an area of risk for material errors, even when management might not think so.
Internal Audit	Internal audit is an independent, objective assurance and consulting activity designed to add value and improve an organization's operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes. It is the functional means by which the managers of an entity receive an assurance from internal sources (including internally subcontracted sources) that the internal controls are achieving their internal control objectives. It will cover, inter alia , Financial Audits, System Based Audits, Performance Audits, IT-Audits
Internal Control	The whole system of financial and other controls, including the organizational structure, methods, procedures and internal audit, established by management within its corporate goals, to assist in conducting the business of the audited entity in a regular, economic, efficient and effective manner.
Internal Control Objective	The primary objectives of internal control are to ensure: <ol style="list-style-type: none"> <li>1. The reliability and integrity of information.</li> <li>2. Compliance with policies, plans, procedures, laws, and regulations.</li> <li>3. The safeguarding of assets.</li> <li>4. The economical, efficient and effective use of resources.</li> </ol> Each organization should design its own system of internal control to meet the needs and environment of the organization.
Performance Audit	An audit of the economy, efficiency and effectiveness with which the audited entity uses its resources in carrying out its responsibilities. In practice, might appear difficulties in distinguishing between performance audit and evaluation. Sometimes the performance audit is limited to the taking into account of the products, but this really limits the real value of the audit. The evaluation can allow the issuing of a data base, especially by using the results, while the performance audit only uses the available information. Performance Audit is usually concerned with testing performance against some given standards.
Public Internal Financial Control (PIFC)	PIFC is the overall financial control system performed internally by a Government or by its delegated organizations, aiming to ensure that the financial management and control of its national budget spending centers (including foreign funds) complies with the relevant legislation, budget descriptions, the principles of sound financial management, transparency, efficiency, effectiveness and economy. PIFC comprises all

	measures to control all government income, expenditure, assets and liabilities. It represents the wide sense of internal control. It includes but is not limited to preventive/ex ante financial control (EAFC) and ex-post internal audit (EPIA)
Risk Analysis	<p>It is an instrument which helps the manager to identify the audit projects which are most favorable to the institution. Risk analysis represents to identify all the local control and financial management systems and to identify the associated risks according to certain risk factors. The risk analysis must be used on at least 2 levels:</p> <ol style="list-style-type: none"> <li>1. to establish the annual audit programs selecting the most favorable projects;</li> <li>2. to plan the effective audit activity.</li> </ol> <p>The risk factors are: data volume evaluation, data importance, control environment, management reliability, and complexity of the activities, Informatics systems, geographical diversity and previous audit knowledge.</p>
Regularity Audit	Attesting the financial liability of the responsible entities which implies the examination and the evaluation of the financial reports and drafting an opinion on the financial statements; attesting the financial liability of the central administration as a whole; the audit of the financial systems and transactions, including an evaluation of compliance with the applicable statutes and regulations, internal control audit, the functions of the internal audit, the audit of the correctness of the administrative decisions of the audited institution, the report of any information that derives from or is connected with the audit and which the Supreme Internal Audit Authority considers that have to be public. This system is not usually used with the internal audit.
System Audit	<p>The System Audit refers to a profound evaluation of the internal control system in order to evaluate if the control functions efficiently. It is designed to appreciate the reliability, the competence of the financial statements, the legality, the regularity of the operations as well as the economy, the efficiency and the efficacy of the operations.</p> <p>A system audit should be followed by profound verifications of the balances and operations in order to find out if the financial statements of the audited institutions are correct and complete, the operations are legally and regularly made and if the economy, the efficiency and the efficacy criteria are fulfilled.</p>

Accountant control	It is systematically practiced by personnel specialized on the financial situations made by the accountant department of the public entity in order to assure the manager that the reported indicators are obtained by registering of the accountant data, according to the good practice rules. IT undertakes the procedures and documents on integrity of the active and passive assets, directing and managing the financial-accountant operations and the reliability of the registered data. It is based on MPF and CHUPIA standards in order to assure the compatibility with the accountant practices in every public entity.
Hierarchical control	Made within the public entities is a permanent type of control made by the each manager on the work results of his employees. It evaluates the way the employees do their work mentioned in the job description, having learning, a evaluating and even a punishing function.
Mutual control	It is an efficient form of control practiced in fazes of a procedural system of each working unit on the working in the previous working unit in order to prepare its own documents and to prepare the control which will be realized in the future working unit.

**ANNEX NO. 2**  
**CURRENT PIFC LEGAL BASIS**

**AS FOLLOWS :**

1. GO no. 119/1999 on internal audit and preventive financial control
2. GEO no. 46/2000 on the modification of letter a), par. (3), art. 7 of GO no. 119/1999 on internal audit and preventive financial control
3. GO no. 85/2000 for the modification and amendment of GO no. 119/1999 on internal audit and preventive financial control
4. Government Resolution no. 164/2000 for the appointment of the chief financial auditor and of the two deputy chief financial auditors
5. GR no. 362/2000 on the organization of internal audit inspection and the determination of its general competencies
6. Ministry of Finance Order no. 33/2000 for the approval of Methodological Standards no. 700.001/2000 on the organization and functioning of the activity of delegate preventive financial control within the Ministry of Finance
7. MFO no. 143/2000 for the approval of the specific framework of documents and operations submitted to delegate preventive financial control exercised on the National Pre-adhesion Fund and PHARE Funds Implementation Agencies
8. MFO no. 332/2000 on General Methodological Standards for the organization and functioning of internal audit
9. MFO no. 492/2000 on the determination of decision competencies on the ascertaining of infringements and enforcement of penalties as per GO no. 119/1999 on internal audit and preventive financial control
10. MFO no. 600/2000 for the approval of the specific framework for documents and operations submitted to the delegate preventive financial control on public treasury budget, public debt and other Ministry of Public Finance specific actions
11. MFO no. 661/2000 on internal audit at the level of the National Fund, Implementation Agencies, Payment Agencies and Implementing Agencies for Community Funds
12. MFO no. 728/2000 for the approval of the modification and amendment of Methodological Standards no. 700.001/2000 for the approval of the modification and amendment of Methodological Standards no. 680.035/2000
13. MFO no. 851/2000 for the approval of the specific framework of documents and operations undergoing delegate preventive financial control on research and development activities
14. MFO no. 1007/2000 for the approval of the specific framework for documents and operations undergoing delegate preventive financial control in the field of Health Houses
15. MFO no. 1013/2000 on stamps and the registration on certification activities by limited authorized audit (accepted persons)
16. MFO no. 1070/2000 on Self Methodological Standards on the organization and functioning of internal audit at the level of the Ministry of Public Finance
17. MFO no. 1097/2000 for the approval of the specific framework for documents and operations undergoing delegate preventive financial control for defense, public order and national security
18. MFO no. 167/2001 on the certification of balance sheets and budget execution accounts for accepted natural or legal persons, for public institutions with less than 25 job positions

19. MFO no. 123/2001 on OPFC Activity Methodological Standards

**ANNEX NO. 3**  
**SCHEDULE OF MEASURE IMPLEMENTATION AS PER POLICY PAPER**

No.	Action	Deadline
<b>A. Short term</b>		
1.	Modification and amendment of legislation (Government Ordinance no. 119/1999 according to Policy Paper provisions	September 2001
2.	Development of the internal audit manual	December 2001
3.	Development of the preventive financial control manual	December 2001
4.	Design of audit trails including for the 2 pre-adhesion financial instruments for ISPA and PHARE	December 2001
5.	Development of the criteria system for the accreditation of controllers	December 2001
6.	Design of methodologies for the risk analyze	March 2002
7.	Design and achievement of commitment computer registration system	March 2002
8.	Development of the Ethical Code of the financial controller /auditor	December 2001
<b>B. Medium Term</b>		
1.	Re-design of general internal audit standards, on the background of international standard enforcement	December 2002
2.	Re-design of preventive control standards	December 2002
3.	Design and performance of controllers certification process	January 2002 – June 2003
4.	Finalization of preventive financial control devolution process	December 2003
5.	Generalization of PIFC structures for all public entities	December 2003
6.	Implementation of Public Internal Financial Control computer system	January 2001 – June 2002
7.	Finalization of de-concentrated process for the ex-ante financial control	December 2003